

Message Text

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ACTION SS-25

INFO OCT-01 ISO-00 SSO-00 /026 W
-----090539Z 126916 /15

R 081439Z JUN 77
FM AMEMBASSY CAIRO
TO SECSTATE WASHDC 5935
INFO AMEMBASSY DAMASCUS
AMEMBASSY JIDDA
AMEMBASSY KUWAIT
ZTN/AMCONSUL ALEXANDRIA UNN

C O N F I D E N T I A L SECTION 1 OF 3 CAIRO 9595

EXDIS

E.O. 11652: GDS
TAGS: EINV, EG
SUBJECT: FORD PROJECT: REPLY TO GOE

REF: CAIRO 9390

1. OUROUSSOFF CALLED AT EMBASSY JUNE 7 TO DELIVER COPY OF FORD LETTER TO GOE (REFTEL). HIS MEETING WITH EL NAZER HAD BEEN VERY SHORT, ALTHOUGH CORDIAL, SINCE LATTER HAD EVIDENTLY JUST BEEN ASKED BY KAISSOUNI TO UNDERTAKE A TRIP ON LATTER'S BEHALF. NAZER DID NOT READ LETTER, ACCORDING TO OUROUSSOFF, BUT WAS TOLD OF ITS GENERAL TONE AND CONTENTS. NAZER FELT THAT IT WAS JUST WHAT IS NEEDED FOR DISCUSSION AT MEETING OF HIGHER INVESTMENT COUNCIL, TO BE HELD ON SOME UNSPECIFIED FUTURE DATE, TO OVER-RIDE OBJECTIONS OF MININD SHAHIN.

2. TEXT OF LETTER, FROM FORD VP WILLIAMS TO DR. KAISSOUNI, IS AS FOLLOWS. BEGIN QUOTE.

DEAR MR. MINISTER:

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I APPRECIATED THE OPPORTUNITY TO MEET WITH YOU IN PARIS LAST MONTH AND TO DISCUSS THE PROPOSED DIESEL ENGINE AND TRUCK MANUFACTURING JOINT VENTURE PROGRAM FOR EGYPT. I FOUND YOUR APPROACH AND THAT OF YOUR ASSOCIATES TOWARD THE STEPS THAT MUST BE TAKEN FOR THE GREATER ECONOMIC WELFARE OF EGYPT TO BE MOST ENCOURAGING. WE AT FORD WOULD LIKE TO BE A PART OF THE DRIVE YOU ARE UNDERTAKING TO RAISE THE LEVEL OF INDUSTRIAL

SKILLS AND, THUS, THE STANDARD OF LIVING IN EGYPT.

DURING OUR MEETING IN PARIS WE AGREED THAT, IN ORDER FOR FORD TO MOVE AHEAD WITH THE DEVELOPMENT OF THE JOINT VENTURE PROGRAM, A NOTE CONFIRMING THE MEMORANDUM OF AGREEMENT, SIGNED BY DR. ADEL GAZARIN AND MYSELF IN CAIRO ON MAY 9, 1977, WOULD BE SENT TO FORD. WE AGREED THAT THIS NOTE WAS TO ACKNOWLEDGE FORMALLY THE APPROVAL OF THE FORD PROJECT BY THE GENERAL AUTHORITY FOR ARAB AND FOREIGN INVESTMENT AND THE FREE ZONES AS INDICATED IN THE ABOVE MEMORANDUM. WE RECOGNIZED THAT SUCH A STEP WAS REQUIRED TO ENABLE FORD TO START CONDUCTING OPERATIONS PROMPTLY IN EGYPT BY ENSURING THAT ALL APPROPRIATE LEVELS OF THE EGYPTIAN GOVERNMENT INVOLVED IN SUCH OPERATIONS WERE AWARE THAT FORD WAS RELEASED FROM THE BOYCOTT IN EGYPT. THIS ACTION WOULD ALSO PERMIT FORD TO PURSUE WITH INCREASED CREDIBILITY AND EFFECTIVENESS THE ACQUISITION OF OTHER ARAB FINANCIAL PARTNERS FOR THE JOINT VENTURE.

I HAVE JUST RECEIVED A LETTER DATED MAY 26 SIGNED BY DR. ALY GAMAL EL NAZER WHICH MAKES NO REFERENCE TO FORD'S REMOVAL FROM THE BOYCOTT IN EGYPT AND WHICH MAKES APPROVAL OF THE PROJECT SUBJECT TO A NUMBER OF ENTIRELY NEW CONDITIONS. IN TOTAL THESE CONDITIONS WILL MAKE THE PROJECT ECONOMICALLY UNWORKABLE FOR REASONS I AM OUTLINING BELOW.

OUR COMMENTS WITH RESPECT TO EACH OF THE SIX NEW CONDITIONS ARE AS FOLLOWS:

1) EGYPTIAN CONDITION: THAT THE EGYPTIAN GOVERNMENT SHALL NOT BEAR AT ANY TIME ANY BURDEN IN FOREIGN CURRENCIES DUE TO THIS
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PROJECT WHETHER IN FINANCING CAPITAL GOODS OR COMPONENTS AND PARTS.

FORD COMMENT: AFTER THE NEW PLANTS WILL HAVE ACHIEVED CAPACITY VOLUMES, THE PROGRAM SHOULD BE SELF-SUFFICIENT IN FOREIGN CURRENCY AND SHOULD NOT REQUIRE FOREIGN CURRENCY ALLOCATIONS. IN THE EARLY YEARS, HOWEVER, THE NEED TO IMPORT CAPITAL GOODS AND REPAY FOREIGN LOANS CAUSES A FOREIGN CURRENCY DEFICIT THAT CANNOT BE HANDLED BY THE JOINT VENTURE; AND WE MUST, THEREFORE, TURN TO THE GOVERNMENT TO PROVIDE FOREIGN CURRENCY ALLOCATIONS. I WANT TO EMPHASIZE, HOWEVER, THAT THESE ALLOCATIONS WOULD BE OFFSET BY SAVINGS VIA IMPORT SUBSTITUTION, AND, CONSEQUENTLY, THE PROJECT WOULD IMPROVE EGYPT'S FOREIGN CURRENCY POSITION IN TOTAL (AS EXPLAINED IN THE PROGRAM BROCHURE AND OUR MARCH 24 LETTER TO DR. MEGUID). THEREFORE, THE GOVERNMENT WOULD NOT BEAR ANY BURDEN IF IMPORT SUBSTITUTION IS INCLUDED IN THE EQUATION. SHOULD THE EGYPTIAN GOVERNMENT BE UNWILLING TO PROVIDE THE REQUIRED FOREIGN EXCHANGE ALLOCATIONS NEEDED IN THE EARLY YEARS OF THE INVESTMENT, THE PROGRAM WOULD NOT BE ECONOMICALLY VIABLE.

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ACTION SS-25

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2) EGYPTIAN CONDITION: THAT THE CUSTOM PROTECTION IN FORM OF DUTIES DIFFERENTIAL BETWEEN CBU PRODUCTS AND IMPORTED COMPONENTS AND PARTS SHALL INCREASE GRADUALLY AS A FUNCTION OF THE LOCAL CONTENT PERCENTAGE. HOWEVER, IT SHOULD BE CLEAR THAT SUCH PROTECTION WILL NOT EXCEED AT ANY TIME THE PROTECTION OFFERED AT PRESENT OR IN THE FUTURE TO EL NASR AUTOMOTIVE MANUFACTURING COMPANY.

FORD COMMENT: THE MEANING OF THIS CONDITION IS UNCLEAR. AS DETAILED IN THE MAY 1976 MEMORANDUM OF UNDERSTANDING, THE PROPOSED SCALE OF DUTIES ON IMPORTED CKD COMPONENTS IS A FUNCTION OF LOCAL CONTENT AND DECREASES TO ZERO AS LOCAL CONTENT INCREASES TO 40 PERCENT. WE AGREE THAT THE PROPOSED DUTIES SHOULD ALSO BE APPLICABLE TO IMPORTS MADE BY OTHER MANUFACTURERS, INCLUDING EL NASR. OUR STUDIES SHOW THAT DUTIES AND TAXES ON ALL IMPORTED BU TRUCKS FROM ANY MANUFACTURER MUST BE INCREASED TO 55 PERCENT AND THE DUTIES AND TAXES ON IMPORTED COMPONENTS MUST BE REDUCED TO ZERO TO ASSURE THE SURVIVAL OF THE INFANT EGYPTIAN TRUCK AND ENGINE MANUFACTURING INDUSTRY. THE PROPOSED PROJECT ASSUMES THAT THE JOINT VENTURE MUST EARN ALL ITS OWN FOREIGN CURRENCY AFTER THE EARLY YEARS. HOWEVER, SHOULD THE EGYPTIAN

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GOVERNMENT ACCEPT A LOWER LEVEL OF EXPORTS GENERATED BY THE PROJECT (AND PROVIDE MORE FOREIGN CURRENCY ALLOCATIONS) THE PROPOSED 55 PERCENT DUTY RATE ON BU TRUCKS COULD BE REDUCED COMMENSURATE WITH SUCH LOWER EXPORT OBJECTIVE.

3) EGYPTIAN CONDITION: THAT FORD WILL FORM IN EGYPT A SALES COMPANY FOR THE PURPOSE OF HANDLING SALES ON A COMMISSION BASIS FOR ALL FORD VEHICLES AND PARTS IN THE AREAS OF THE WORLD DESCRIBED ON PAGE 4 OF THE MARCH 24, 1977 LETTER.

FORD COMMENT: AS OUTLINED IN OUR MARCH 24 LETTER, IT IS OUR INTENT TO RECOMMEND TO OUR MANAGEMENT AS PART OF THE TOTAL JOINT VENTURE PROGRAM THE FORMATION OF THE DESCRIBED SALES COMPANY, SUBJECT TO SATISFACTORY RESOLUTION OF THE RELATED TAX AND LEGAL ISSUES.

4) EGYPTIAN CONDITION: THAT FORD PARTICIPATION IN THE PAID CAPITAL OF THE PROJECT SHALL NOT BE LESS THAN 5 MILLION DOLLARS IN ADDITION TO THE PRESENT FORD PLANT IN SMOUHA, ALEXANDRIA, WHICH WILL BE EVALUATED ON BASIS TO BE APPROVED BY THE AUTHORITY.

FORD COMMENT: ASSUMING THAT THE VALUATION BASIS APPROVED BY THE AUTHORITY WOULD RESULT IN AN APPRAISED VALUE OF THE FACILITY THAT REFLECTS ITS REAL VALUE, AND THE EGYPTIAN GOVERNMENT AND OTHER PROSPECTIVE PARTNERS WOULD SUPPLY THE REMAINING 70 PERCENT EQUITY IN CONVERTIBLE CURRENCY, WE WOULD AGREE TO RECOMMEND TO OUR MANAGEMENT THE PROPOSED CONDITION. IT SHOULD BE NOTED, HOWEVER, THAT AN INCREASE IN EQUITY LEVELS WILL REQUIRE HIGHER PROFITS TO MAINTAIN A RATE OF RETURN ACCEPTABLE TO OUTSIDE INVESTORS, AND THEREFORE, WE BELIEVE, IT IS NOT IN THE BEST INTEREST OF EGYPT.

5) EGYPTIAN CONDITION: THE PROJECT SHOULD FORESEE THE GRADUAL INCREASE OF THE LOCAL CONTENT OF BOTH THE TRUCK AND DIESEL ENGINE. A MINIMUM LOCAL CONTENT OF 70 PERCENT IN VALUE OF THE COMPLETE PRODUCT SHOULD BE PLANNED AND THE CONFIDENTIAL

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NECESSARY INVESTMENT SHOULD BE EVALUATED AND INCLUDED IN THE PROJECT, WITH THE TIME SCHEDULE FOR THE PROGRESS OF THE DIFFERENT PRODUCTION STAGES.

FORD COMMENT: AS OUTLINED IN THE PROGRAM BROCHURE THE PROGRAM OBJECTIVE IS TO ACHIEVE 40 PERCENT LOCAL CONTENT BY THE FOURTH YEAR FOLLOWING STARTUP OF THE PROGRAM. THIS OBJECTIVE WAS DETERMINED AFTER A CAREFUL EVALUATION OF THE PRESENT AND POTENTIAL AVAILABILITY OF LOCAL MATERIAL AND COMPONENTS AND INVESTMENT REQUIREMENTS.

OUR OVERALL OBJECTIVE IS TO MAXIMIZE LOCAL CONTENT AND THEREBY REDUCE FOREIGN CURRENCY REQUIREMENTS, BUT ONLY ON AN ECONOMICALLY VIABLE BASIS. TO INCREASE THE OBJECTIVE TO 70 PERCENT NOW WOULD REQUIRE SUBSTANTIALLY HIGHER INVESTMENTS AND INCREASED COSTS, THEREBY REQUIRING SUBSTANTIALLY HIGHER PRICES FOR TRUCKS TO BE SOLD IN EGYPT. WE DO NOT BELIEVE THIS IS A REASONABLE COURSE OF ACTION AT THIS TIME. WE WOULD, HOWEVER, CONTINUALLY ATTEMPT TO INCREASE LOCAL CONTENT AS THE PROGRAM DEVELOPS IN EGYPT AND AS IT BECOMES ECONOMICALLY FEASIBLE.

IN OUR VIEW, A 40 PERCENT LOCAL CONTENT OBJECTIVE IS A CHALLENGING, BUT ACHIEVABLE OBJECTIVE SUPPORTED BY THE EXISTING AND ANTICIPATED MATERIAL SUPPLY BASE IN EGYPT, AND IT WOULD BE UNREALISTIC TO COMMIT TO A HIGHER OBJECTIVE AT THIS TIME.

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6) EGYPTIAN CONDITION: THE SALES PRICE FOR THE DIESEL ENGINES AND THE TRUCKS IN EGYPT SHOULD BE WITHIN COMPETITIVE INTERNATIONAL PRICES OF SIMILAR IMPORTED PRODUCTS. THE EGYPTIAN CONSUMER SHOULD BEAR NO PENALTY IN FORM OF HIGHER PRICES IMPOSED ON THE LOCALLY BUILT PRODUCT.

FORD COMMENT: IT MUST BE RECOGNIZED THAT FROM A MANUFACTURING COST VIEWPOINT THERE IS NO WAY THAT A NEW TRUCK OR ENGINE MANUFACTURING OPERATION IN EGYPT CAN MATCH THE MANUFACTURING COSTS OF HIGH VOLUME PLANTS ALREADY ESTABLISHED IN OTHER PARTS OF THE WORLD. TO ASSURE THE NEW INDUSTRY ADEQUATE

SALES VOLUMES, AND TO OFFSET THE COST DIFFERENCES BETWEEN THE NEW PLANTS AND ALREADY ESTABLISHED PLANTS, THE GOVERNMENT MUST PROVIDE A DUTY DIFFERENTIAL BETWEEN IMPORTED BU AND LOCALLY MANUFACTURED CKD VEHICLES. BECAUSE THE PROPOSED PROJECT IS ALSO BURDENED WITH AN EXPORT OBJECTIVE TO GENERATE FOREIGN CURRENCY EARNINGS TO PAY FOR COMPONENTS IT IMPORTS, THE REQUIRED PROTECTION MUST BE HIGHER THAN IF EXPORTS WERE NOT REQUIRED. SHOULD THE GOVERNMENT WANT TO KEEP CONSUMER PRICES ARTIFICIALLY LOW, IT WOULD HAVE TO SUBSIDIZE THE MANUFACTURER IN A DIFFERENT WAY --E.G., EXPORT SUBSIDIES.

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THE PRICING FORMULAE INCLUDED IN THE PROGRAM WERE PROPOSED AFTER MANY DISCUSSIONS WITH THE EGYPTIAN COMMITTEE AND, WE BELIEVE, REPRESENT A GOOD COMPROMISE BETWEEN GOVERNMENT, CONSUMER, AND JOINT VENTURE INTERESTS, WHICH WILL, OVER THE LONG RUN, MAXIMIZE THE BENEFITS TO ALL PARTIES.

BECAUSE WE HAVE DISCUSSED THESE MATTERS IN SUCH DETAIL AT VARIOUS LEVELS WITH THE EGYPTIAN GOVERNMENT, CULMINATING IN OUR MEETINGS IN PARIS IN MAY, FRANKLY, WE ARE PUZZLED AABOUT THESE NEW CONDITIONS. AS I HAVE OUTLINED ABOVE, THEIR EFFECT WULD BE TO MAKE THE PROJECT ECONOMICALLY UNVIAIBLE. WE URGE YOUR CONSIDERATION OF THE ABOVE CONDITIONS AND A RETURN TO THE LEVEL OF UNDERSTANDING ENCOMPASSED IN THE MEMORANDUM OF AGREEMENT OF MAY 9, 1977. WE ARE PREPARED, ON THE BASIS OF THAT MEMORANDUM OF AGREEMENT, TO PROCEED WITH FURTHER DEVELOPMENT OF THE PROJECT.

IF THE GOVERNMENT OF EGYPT CAN AGREE TO THIS POSITION, IT IS ALSO OF CRITICAL IMPORTANCE THAT FORD BE REMOVED FROM THE BOYCOTT IN EGYPT FOR THE REASONS AGREED UPON IN OUR PARIS MEETING.

WE STAND READY TO RESPOND IN ALL SUITABLE WAYS, INCLUDING A RETURN TO EGYPT, TO ANY REQUEST YOU MAY HAVE FOR FURTHER INFORMATION OR DETAIL REGARDING THE ITEMS IN THE PROGRAM. PERHAPS OUR LOCAL GENERAL MANAGER, MR. NICHOLAS OUROUSSOFF, WHO IS THOROUGHLY FAMILIAR WITH THE REQUIREMENTS FOR THE PROGRAM, COULD BE OF ASSISTANCE TO YOUR COLLEAGUES ON A LOCAL BASIS.

WE ARE MOST ANXIOUS TO COME TO AN EARLY CONCLUSION ON THESE MATTERS AND CLEAR UP WHAT APPEAR TO BE MISUNDERSTANDINGS.

END QUOTE.

3. COMMENT: OUROUSSOFF SAYS LETTER IS INTENDED TO BE REASONABLE REPLY TO UNREASONABLE REQUEST, DESIGNED TO SHOW THAT FORD IS WILLING TO MOVE AHEAD WITH PROJECT AS SOON AS EXTRANEIOUS

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OBSTACLES ARE REMOVED--AND COMPANY IS REMOVED FROM BLACKLIST
IN EGYPT. HE SEEMS REASONABLY CONFIDENT THAT GOE WILL ACCEPT
LETTER IN THAT LIGHT, AND AGREES THAT THERE ARE STILL A FEW
AREAS OF PROPOSAL THAT NEED TO BE SETTLED BEFORE PROJECT
CAN BE CONSIDERED ON THE RAILS. HOME OFFICE APPEARS TO BE
RATHER OPTIMISTIC: OUROUSSOFF HAS BEEN INSTRUCTED TO FIND
12 DEALERS IN EGYPT BY JULY 1.
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Message Attributes

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Decaption Date: 22 May 2009
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
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Disposition Reason:
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